GOVERNOR'S OFFICE OF BUDGET AND PROGRAM PLANNING

Fiscal Note 2009 Biennium

Bill #	SB0515		**Title:**	Contingent reduction of income tax rates based upon surplus revenue
Primary Sponsor:	Balyeat, Joe		**Status:**	As Introduced

- ☐ Significant Local Gov Impact
- ☐ Needs to be included in HB 2
- ☑ Technical Concerns
- ☐ Included in the Executive Budget
- ☑ Significant Long-Term Impacts
- ☐ Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2008 Difference	FY 2009 Difference	FY 2010 Difference	FY 2011 Difference
Expenditures:				
General Fund	$0	$0	$0	$0
Revenue:				
General Fund	$0	$0	$0	$0
Net Impact-General Fund Balance:	$0	$0	$0	$0

Description of fiscal impact:

This bill will reduce income tax rates for the calendar year beginning after every fiscal year in which income tax collections are more than 3% higher than the HJR 2 individual income tax forecast. Based on recent history, this contingency is likely to occur at least once every other biennium. Each occurrence will reduce income tax revenue by tens of millions of dollars with the long term impact likely to be in the hundreds of millions of dollars.

FISCAL ANALYSIS

Assumptions:

1. At the end of each fiscal year, beginning with FY 2008, this bill would require the Department of Administration to certify the amount by which individual income tax collections, exclusive of audit collections and amended returns attributable to a tax year that began before the tax year in which the fiscal year began exceeds the HJR 2 individual income tax revenue estimate, exclusive of the amount attributable to audit collections.
2. If the amount certified in assumption 1 is at least 3% more than estimated in HJR 2, the income tax rates in 15-30-103, MCA, will be reduced, beginning the next tax year, by the percent difference certified by the State Treasurer.
3. It is assumed that the comparison in this bill is to be between actual revenue and the latest revenue forecast (see Technical Note 1).

4. The following table: (1) shows actual income tax revenue for FY 2000 through FY 2006 and the HJR 2 revenue estimates for these years and (2) shows the percent difference between actual revenue collected to the last HJR 2 revenue estimate adopted for each fiscal year.

Individual Income Tax Revenue Collections Versus HJR 2 Projections (not adjusting for the prior year revenue or the estimated audit collections) ($ million)

	Date of Forecast	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006
Actual Revenue		$516.262	$556.015	$517.568	$535.831	$605.582	$707.343	$768.922
Session								
1999 Regular	April 1999	$475.687	$496.634					
2000 Special	May 2000	$511.099	$531.786					
2001 Regular	April 2001		$545.356	$575.077	$598.531			
2002 Special	Aug. 2002				$527.919			
2003 Regular	April 2003				$520.764	$556.874	$594.339	
2005 Regular	April 2005						$619.486	$605.029
2005 Special	Dec. 2005							$677.815

Comparison of Income Tax Revenue Collections versus Final HJR 2 Projections ($ million)

	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005	FY 2006
Actual Revenue	$516.262	$556.015	$517.568	$535.831	$605.582	$707.343	$768.922
Latest Forecast	$511.099	$545.356	$575.077	$520.764	$556.874	$619.486	$677.815
% Difference	1.0%	2.0%	-10.0%	2.9%	8.7%	14.2%	13.4%

The contingency in this bill would have been met in three of the last seven fiscal years, and the average percentage difference between actual and forecast revenue is 4.6% after adjusting the revenue estimates in three special sessions.

5. It is likely that the contingency in this bill will be met at least once in the next four fiscal years. For illustrative purposes, impacts were estimated for income tax revenue exceeding the forecast in FY 2010 by the minimum amount to trigger a rate reduction, 3%, the average amount for the last seven years, 4.6%, and by the highest amount for the last seven years, 14.2%. The income tax forecasting model was run with the 2011 rates reduced by 3%, 4.6% and 14.2%. Compared to the same model with current law rates, full year resident tax liability for 2011 was lower by $25.800 million in the first case, by $39.422 million in the second case, and by $120.554 million in the third case. Since the change would occur in the middle of FY 2011, the revenue impact in FY 2011 would be about half the reduction in calendar year tax liability.
6. For any year when income tax rates changed because of this bill, the Department of Revenue would revise withholding tables and mail the revised tables to approximately 40,000 businesses. The cost for printing and mailing would be $20,820.

Effect on County or Other Local Revenues or Expenditures:

1. None.

Long-Range Impacts:

1. Under this bill, income tax rates would continue to be cut every few years. The impact of each individual rate reduction would grow over time as income grows. Each time the contingency in this bill is met, rates would be reduced further, with the impact of that rate cut being added on top of previous impacts.
2. If a cut of $39.4 million occurred in 2011 and every four year after that and the impact of each cut grew by 3% per year, the impact in 2026 would be $207.4 million.
3. If the individual cuts were $120.6 million, the impact in 2026 would be $634.9 million.

Technical Notes:

1. When the legislature adopts revenue estimates in HJR 2, it adopts estimates for three fiscal years: the current fiscal year and the two years of the coming biennium. Thus, the legislature, meeting in regular session, adopts two estimates of income tax revenue for odd numbered fiscal years, one approximately fifteen months before the fiscal year begins and another three to four months before its end. In addition, when the legislature meets in special session, it generally adopts new revenue estimates. The bill does not specify which of the two or more estimates the legislature adopts is to be used for the comparison with actual collections. This fiscal note assumes that the one most recently adopted should be used, but this should be clarified. If the comparison were to be based on the original estimate, the contingency in this bill would have been met in five of the last seven years.
2. Section 2(2) requires that on occurrence of a contingency, income tax rates "must be reduced by the percentage amount that individual income tax collections ... exceeded the amount estimated by the legislature." This fiscal note assumes this means that if collections exceed the forecast by X%, then the rates in 15-30-103, MCA, are to be multiplied by 1-X%, not that X% is to be subtracted from each rate.
3. Section 2(2) requires a comparison of "individual income tax collections, excluding amended returns and audit collections attributable to a tax year that began before the tax year in which the fiscal year began" with income tax revenue "estimated by the legislature, as provided in 5-5-227, MCA, exclusive of the amount attributable to audit collections." The Department of Revenue records parts of income tax collections as audit revenue and revenue from prior year and amended returns. The Legislative Fiscal Division generally attributes part of the HJR 2 income tax revenue estimate to audit collections. It is not clear that these are comparable or that either is the same as the revenue that this bill would require to be taken out of actual and projected revenues before comparing them. This bill should either specify in more detail what is to be excluded from the projections and certified collections or provide rule making authority.
4. Section 3 requires the State Treasurer, i.e. Director of the Department of Administration (see 2-15-1002, MCA), to:
    - adjust the legislative forecast for income tax revenue adopted in HJR 2 for legislation,
    - certify the amount and percentage by which income tax collections exceeds the adjusted forecast, and
    - notify the Secretary of State, the Department of Revenue, the Code Commissioner, and the Legislative Fiscal Division.
        a. The HJR 2 forecast currently is adjusted for legislation by the Legislative Fiscal Division, in consultation with the Office of Budget and Program Planning. Requiring the Department of Administration to perform the same function would be an unnecessary duplication of effort, and, since this adjustment requires the exercise of professional judgment, could result in inconsistent adjusted revenue projections.
        b. Section 3 does not specify when the Department of Administration is to certify income tax collections for a fiscal year. Presumably, this would be done as part of the preparation of the Comprehensive Annual Financial Report, but if the certification is to result in lower income tax rates beginning January 1, it would be good to have a definite timeline.

   c. It also is not clear whether the "collections" that are to be certified are cash receipts or fiscal year revenue, which includes amounts due at the end of the fiscal year and collected later.
   d. Income tax revenue may exceed projections in a year when overall revenue is less than projected. Since the governor is charged with reducing spending in the event of a projected budget shortfall, the Director of the Office of Budget and Program Planning should also be notified.
5. The Department of Administration's current functions do not have an audit function which would allow the State Treasurer to certify the numbers required by this bill. It may be more appropriate to define an agency with audit staff to certify these numbers.

Sponsor's Initials	*Date*	*Budget Director's Initials*	*Date*